

Congress of the United States
CONGRESSIONAL OVERSIGHT PANEL

Opening Statement of J. Mark McWatters

Congressional Oversight Panel Hearing on the Use of Private Contractors in the TARP

September 22, 2010

Thank you Mr. Silvers.

I very much appreciate the attendance of the witnesses and I look forward to hearing their views.

The Department of Treasury is authorized under the Emergency Economic Stabilization Act of 2008 (EESA) to enter into “procurement contracts” and “financial agency agreements (FAA)” in order to discharge its duties under the statute.¹ Financial agency agreements allow Treasury to retain financial institutions to perform “inherently governmental” and, perhaps, other functions, and procurement contracts are employed by Treasury to obtain other goods and services from private sector organizations.² Today’s hearing will examine Treasury’s use of procurement contracts and financial agency agreements to obtain services that Treasury cannot, or has chosen not to, perform itself.

In order to add some perspective to the materiality of the issues before us today, it is worth considering that the potential value of procurement contracts between Treasury and third-party service providers totals approximately \$400 million, roughly \$85 million of which relates to “limited competition” contracts issued due to “unusual and compelling urgency.”³ It will be interesting to learn the circumstances that justified the issuance of the limited competition contracts as well as why only four service providers account for \$79 million of the \$127 million in obligated value attributable to all the procurement contracts.⁴

¹ 12 U.S.C. 5211(c).

² The adoption of EESA introduced an element of legal uncertainty as to whether financial agency agreements must be used only for “inherently governmental” functions or if they can be used for a broader range of duties as well. As a result, there may be essentially no restrictions on the process Treasury may use for selecting financial institutions as financial agents. Unlike when it hires a contractor, an executive agency is not bound by the Federal Acquisition Regulations (FAR) when it hires a financial agent. The law, however, is well-settled that a financial agent must abide by the principles of agency law, as the financial agent acts an agent for the government, the principal. As a result, the duties that would attach in any other principal-agent relationship attach to financial agents, including the duty of loyalty and the duty of care.

³ These amounts represent estimates obtained by Panel staff as of August 13, 2010.

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It is also worth noting that Treasury has entered into financial agency agreements with Fannie Mae and Freddie Mac that have an obligated value of approximately \$220 million.⁵ Since Fannie and Freddie were all but nationalized⁶ in September 2008 it will be interesting to learn why Treasury chose to enter into significant contractual arrangements with two failed government-sponsored enterprises (GSEs) instead of with solvent private sector organizations, and if Treasury was able to secure services from the GSEs on “arm’s length” terms. Since Treasury also engaged Fannie and Freddie to modify non-HAMP (Home Affordable Modification Program), GSE owned or guaranteed loans, it is critical that the two GSEs address how they mitigated any conflicts of interest that have arisen with respect to their financial agency agreements.

EESA requires Treasury to establish and maintain an effective system of internal controls to provide reasonable assurance of “the effectiveness and efficiency of operations, including the use of the resources of the TARP,” “the reliability of financial reporting, including financial statements and other reports for internal and external use,” and “the compliance with applicable laws and regulations.”⁷ In addition, fundamental elements of this Panel’s mandate are to examine the “extent to which the information made available on transactions under the [TARP] has contributed to market transparency,”⁸ and to ensure that the use of TARP authority is subject to “public accountability.”⁹ As such, one goal of today’s hearing is to determine if Treasury, the procurement contractors and the financial agents have adopted a set of “best practices” with respect to the development and implementation of their internal control systems and have taken such other necessary and appropriate actions so as to ensure market transparency and public accountability regarding their procurement contracts and financial agency agreements.

EESA also requires the Secretary of the Treasury to issue “regulations or guidelines necessary to address and manage or to prohibit conflicts of interest that may arise in connection with the administration and execution” of the statute.¹⁰ Although on January 21, 2009, Treasury adopted an Interim Final Rule (IFR) regarding conflicts of interest arising with respect to procurement contracts and financial agency agreements,¹¹ several questions remain for analysis. For example, real or perceived conflicts of interest may arise under any of the following four circumstances:

⁵ This amount represents an estimate obtained by Panel staff. It is current as of August 13, 2010.

⁶ The Congressional Budget Office (CBO) estimates that the total subsidy cost for the bailout of Fannie Mae and Freddie Mac will total approximately \$389 billion through 2019. Congressional Budget Office, *Budgetary Treatment of Fannie Mae and Freddie Mac*, at 8 (Jan. 2010) (online at www.cbo.gov/ftpdocs/108xx/doc10878/01-13-FannieFreddie.pdf).

⁷ 12 U.S.C. § 5226(c)(1)(A)-(C).

⁸ 12 U.S.C. § 5233(b)(1)(A)(iii).

⁹ 12 U.S.C. § 5201(2).

¹⁰ 12 U.S.C. § 5218(a).

¹¹ TARP Conflicts of Interest, 74 Fed. Reg. 3431-3436 (Jan. 21, 2009) (codified as 31 CFR § 31). This Interim Final Rule followed Treasury’s issuance of the Interim Guidelines for Conflicts of Interest on October 6, 2008, only three days after the passage of EESA. U.S. Department of the Treasury, Interim Guidelines for Conflicts

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- Treasury contracts with a firm and then seeks to regulate the firm or its industry.
- Treasury enters into an arrangement with a contractor or financial agent – or that contractor or financial agent enters into an arrangement with a subcontractor – and subsequently intends to hire an employee from one of those retained entities.
- Treasury develops an overreliance on one specific firm because it has entered multiple arrangements with that firm.
- Treasury hires a contractor or financial agent – or that contractor or financial agent hires a subcontractor – that needs government support in the future.”

It will be helpful to learn this morning how Treasury intends to address each of these conflict of interest issues.

Thank you for joining us today and I look forward to our discussion.

of Interest (Oct. 6, 2008) (online at www.treas.gov/press/releases/hp1180.htm). Treasury has not yet issued a final rule.